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Muni-Bond Liquidity Crisis Hits Governments With Rates Up to 11%.

- **Sell-off in variable-rate bonds as managers meet redemptions**
- **Shades of 2008 crisis, with billions of bonds resetting higher**

The sell-off sweeping through the municipal-bond market is hitting cities, public-transit systems, hospitals and local governments with spiraling interest bills on floating-rate debt, dealing a new financial hit just as they contend with the economic toll of the coronavirus pandemic.

The jump is a result of the rapid pullback from the market over the last two weeks, which has left mutual-fund managers dumping the most liquid securities to raise cash to cover investors' withdrawals. The variable-rate bonds are among the easiest to offload because they can always be sold at full face value to Wall Street banks, which have been forced to reset the interest rates sharply higher to avoid being stuck with unwanted inventories.

"If you're a portfolio manager and you need cash — or you think you will need cash and you want to get ahead of the curve, you're going to sell whatever is the most liquid," said Patrick Luby, who tracks the municipal market for CreditSights Inc.

The pressure has driven up the yields on tens of billions of dollars of bonds by the most since the market froze up during the 2008 credit crisis. Those on debt issued by New York's Metropolitan Transportation Authority, which is seeking a federal bailout after subway and train travel tumbled, jumped to 9% when they reset Thursday, up from around 1% last week, according to data compiled by Bloomberg. Dozens of other bond issues have seen similar increases, including those sold by Indianapolis, the Columbus, Ohio airport and New York's water system. Those issued by Maryland's industrial development authority for Occidental Petroleum Corp. hit 11%.

The hikes come as Wall Street's municipal-bond desks are dealt blow after blow, with state and local debt headed for the worst monthly rout since 1984, according to Bloomberg Barclays indexes. With investors pulling money, managers are racing to raise cash.

Variable-rate municipal bond are one of the easiest investments to unload because they can always be sold at 100 cents on the dollar as frequently as every day, allowing fund managers to avoid locking in losses if they instead sold longer-dated securities that have fallen steeply during last two weeks. Banks are required to buy the securities if there aren't enough buyers, giving them a strong incentive to raise the rates so they don't have to hold the debt themselves.

The rising rates echo what happened in 2008, when much of the variable-rate municipal market unraveled after the real estate bubble burst. The market for so-called auction-rate securities collapsed completely as investors dumped them en masse, while the yields on other bonds surged.

The sell-off is coming just as banks' inventories of the securities usually swell around this time of the year as Americans sell them in order to pay their tax bills.

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